



## **24 CFR Parts 203 and 206**

**[Docket No. FR-6151-P-02]**

**RIN 2502-AJ51**

### **Adjustable Rate Mortgages: Transitioning from LIBOR to Alternate Indices**

**AGENCY:** Office of Housing, U.S. Department of Housing and Urban Development (HUD).

**ACTION:** Proposed rule.

**SUMMARY:** HUD is proposing to remove the London Interbank Offered Rate (LIBOR) as an approved index for adjustable interest rate mortgages (ARMs), and replace LIBOR with the Secured Overnight Financing Rate (SOFR) as a Secretary-approved index for newly originated forward ARMs. HUD also proposes to codify its removal of LIBOR and approval of SOFR as an index for newly-originated Home Equity Conversion Mortgage (HECM or reverse mortgage) ARMs. In addition, HUD is proposing to establish a spread-adjusted SOFR index as the Secretary-approved replacement index to transition existing forward and HECM ARMs off LIBOR. HUD also proposes to make clarifying changes to its HECM Monthly ARM regulation and establish a lifetime five percent interest rate cap for monthly adjustable rate HECMs.

**DATES:** Public comment due date: **[Please insert date that is 30 days after the date of publication in the Federal Register]**.

**ADDRESSES:** Interested persons are invited to submit comments regarding this proposed rule to the Regulations Division, Office of General Counsel, Department of Housing and Urban Development, 451 7th Street, SW, Room 10276, Washington, DC 20410-0500. Communications must refer to the above docket number and title. There are two methods for submitting public comments. All submissions must refer to the above docket number and title.

**1. Submission of Comments by Mail.** Comments may be submitted by mail to the Regulations Division, Office of General Counsel, Department of Housing and Urban Development, 451 7th Street, SW, Room 10276, Washington, DC 20410-0500. Due to security

measures at all federal agencies, however, submission of comments by standard mail often results in delayed delivery. To ensure timely receipt of comments, HUD recommends that comments submitted by standard mail be submitted at least two weeks in advance of the deadline. HUD will make all comments received by mail available to the public at <https://www.regulations.gov>.

**2. Electronic Submission of Comments.** Interested persons may submit comments electronically through the Federal eRulemaking Portal at [www.regulations.gov](http://www.regulations.gov). HUD strongly encourages commenters to submit comments electronically. Electronic submission of comments allows the commenter maximum time to prepare and submit a comment, ensures timely receipt by HUD, and enables HUD to make them immediately available to the public. Comments submitted electronically through the [www.regulations.gov](http://www.regulations.gov) website can be viewed by other commenters and interested members of the public. Commenters should follow the instructions provided on that site to submit comments electronically.

**Note:** To receive consideration as public comments, comments must be submitted through one of the two methods specified above. Again, all submissions must refer to the docket number and title of the rule.

*No Facsimile Comments.* Facsimile (FAX) comments are not acceptable.

**Public Inspection of Public Comments.** All properly submitted comments and communications submitted to HUD will be available for public inspection and copying between 8 a.m. and 5 p.m. weekdays at the above address. Due to security measures at the HUD Headquarters building, an advance appointment to review the public comments must be scheduled by calling the Regulations Division at 202-402-3055 (this is not a toll-free number). Individuals can dial 7-1-1 to access the Telecommunications Relay Service (TRS), which permits users to make text-based calls, including Text Telephone (TTY) and Speech to Speech (STS) calls. Copies of all comments submitted are available for inspection and downloading at [www.regulations.gov](http://www.regulations.gov).

## **FOR FURTHER INFORMATION CONTACT:**

Lisa Saunders, Office of Housing, Department of Housing and Urban Development, 451 7th Street, SW, Washington, DC 20410-8000; telephone number 202-402-2378 (this is not a toll-free number); email address [sffeedback@hud.gov](mailto:sffeedback@hud.gov). Individuals can dial 7-1-1 to access the Telecommunications Relay Service (TRS), which permits users to make text-based calls, including Text Telephone (TTY) and Speech to Speech (STS) calls. Individuals who require an alternative aid or service to communicate effectively with HUD should email the point of contact listed above and provide a brief description of their preferred method of communication.

## **SUPPLEMENTARY INFORMATION:**

### **I. Background**

#### *Statutory provisions*

Section 251(a) of the National Housing Act (NHA) (12 U.S.C. 1715z-16(a)) authorizes HUD to insure ARMs and provides that adjustments to the interest rate shall correspond to a specified interest rate index approved in regulations by the Secretary, information on which must be readily accessible to mortgagors from generally available published sources. For HECMs, Section 255(d) of the NHA (12 U.S.C. 1715z- 20(d)) authorizes FHA to insure variable rate HECMs and imposes additional eligibility requirements on HECMs, which include requirements for HECM ARMs.

#### *Forward ARMs*

HUD initially provided for mortgage insurance of ARMs for single family forward mortgages under 24 CFR part 203 and for part 234 condominium mortgages in 1984.<sup>1</sup> As provided in the statute at that time, the interest rate on ARMs had to be adjusted annually, and there was a 1 percent cap on annual adjustments and an overall cap of 5 percent above the initial interest rate over the term of the mortgage. The index originally used by HUD was the U.S. Constant Maturity Treasury (CMT). In 2001 and 2003, statutory changes to Section 251 of the

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<sup>1</sup> 49 FR 23580, June 6, 1984.

NHA, 12 U.S.C. 1715z–16 allowed HUD to insure ARMs that have fixed interest rates for 3 years or more and are not subject to interest rate caps if the interest rate remains fixed for more than 3 years.<sup>2</sup> In 2004, HUD issued a rule (“the 2004 rule”) implementing these statutory changes and providing mortgage insurance for forward ARMs with interest rates first adjustable in 1 year, 3 years, 5 years, 7 years, and 10 years.<sup>3</sup>

Under the 2004 rule, 1, 3, and 5-year ARMs were capped, for each adjustment, in either direction at one percentage point from the interest rate in effect for the period immediately preceding the adjustment. For the life of the mortgage, the overall 5 percent cap in either direction remained. For 7 and 10-year ARMs, HUD raised the per-adjustment cap to 2 percent of the rate in effect for the immediately preceding period, and the life-of-mortgage cap to 6 percent. In all cases, changes that exceeded these amounts could not be carried over for inclusion in an adjustment for the subsequent year. In 2005, HUD revised the regulation to allow for annual adjustments of 2 percent change in either direction, and a life-of-mortgage cap of 6 percent in either direction for 5-year ARMs in 2005, conforming 5-year ARMs to HUD’s 7 and 10-year ARM products.<sup>4</sup>

In 2007 (“the 2007 rule”), HUD added LIBOR, along with the CMT, as an acceptable index for ARM adjustments for its ARM products.<sup>5</sup> For forward mortgages, the applicability of these indices is codified at 24 CFR 203.49. The cap on 1 and 3-year ARMs (no more than 1 percent in either direction per single adjustment, with a 5 percent from initial contract rate cap over the life of the loan) is codified at § 203.49(f)(1). The caps for the 5, 7 and 10-year ARMs (2 percent in either direction per adjustment, with a 6 percent from initial contract rate cap for the life of the mortgage) are codified at § 203.49(f)(2). HUD also created model note and mortgage

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<sup>2</sup> Departments of Veterans Affairs and Housing and Urban Development, and Independent Agencies Appropriations Act, 2002 (Pub. L. 107–73, approved November 26, 2001); HOPE VI Program Reauthorization and Small Community Main Street Rejuvenation and Housing Act of 2003 (Pub. L. 108-186, 117 Stat. 2685, approved December 16, 2003).

<sup>3</sup> 69 FR 11500, March 10, 2004.

<sup>4</sup> 70 FR 16080, March 29, 2005.

<sup>5</sup> 72 FR 40047, July 20, 2007.

documents for forward ARMs and revised those model documents over the years. The 2015 Model ARM Note<sup>6</sup> contains a provision for the substitution of an index by the note holder based on “comparable information,” should the index specified in the note become unavailable.

#### *Reverse mortgages or HECMs*

In 1989, the Home Equity Conversion Mortgage program rule (the HECM rule) provided for ARMs with both capped and uncapped interest rate adjustments.<sup>7</sup> For capped HECM ARMs, the HECM rule retained the 5 percentage point life-of-mortgage limit on interest rate increases and decreases in § 203.49, but increased the annual limit on rate increases and decreases from 1 percentage point to 2 percentage points. The HECM rule also provided for a HECM ARM that sets a maximum interest rate that could be charged without a cap on monthly or annual increases or decreases.

In the 2007 rule, in which LIBOR was added for forward mortgages, HUD also added LIBOR as an acceptable index for HECM ARM adjustments in current §§ 206.3 (definitions) and 206.21 (interest rate).<sup>8</sup> HUD’s model HECM ARM note and mortgage documents have been revised over the years, but the 2015 version contains provisions for the substitution of a Secretary-prescribed index, should the index specified in the note become unavailable.<sup>9</sup>

For the capped option at § 206.21(b)(1), the interest rate cap structure is the same as provided in forward mortgages under § 203.49(a), (b), (d), and (f), except that under § 203.49(d), the reference to first debt service payment means the closing in the HECM ARM context, and under § 203.49(f)(1), the cap on adjustments for one- and three-year mortgages is 2 percentage points in the HECM ARM context. Section 206.21(b)(1)(ii) applies the LIBOR and CMT index options in the same manner as forward ARMs at § 203.49(b) for both the capped and uncapped options. In addition, the uncapped option at § 206.21(b)(2) includes options to adjust based on

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<sup>6</sup> The 2015 Model ARM Note is available on HUD’s website at: [https://www.hud.gov/program\\_offices/housing/sfh/model\\_documents](https://www.hud.gov/program_offices/housing/sfh/model_documents).

<sup>7</sup> 54 FR 24822, June 9, 1989.

<sup>8</sup> 72 FR 40048, July 20, 2007.

<sup>9</sup> The 2015 Model ARM Note is available on HUD’s website at: [https://www.hud.gov/program\\_offices/housing/sfh/model\\_documents](https://www.hud.gov/program_offices/housing/sfh/model_documents).

the one-month CMT or one-month LIBOR index. Section 206.21(b)(1)(iii) also includes ARM interest rate adjustment options for HECMs in the same manner as forward mortgages at § 203.49(d).

On March 11, 2021, in Mortgagee Letter 2021–08, HUD removed LIBOR as an approved index and approved the SOFR index for annually adjustable HECM ARMs closed on or after May 3, 2021.<sup>10</sup> A mortgagee may set rates using CMT or SOFR for annually adjustable HECM ARMs and CMT only for monthly adjustable HECM ARMs. Also, among other changes to the ARM requirements in the Mortgagee Letter, HUD published revised model mortgage documents with “fallback” language intended to address future interest rate index transition events. This language was modeled after the Alternative Reference Rates Committee’s (ARRC)<sup>11</sup> published fallback language for residential ARMs.<sup>12</sup>

#### *Phase-out of LIBOR*

The financial industry is transitioning from use of the LIBOR index given its increasing unreliability and speculative nature. As noted by the Financial Stability Oversight Council, the scarcity of underlying transactions makes LIBOR potentially unsustainable, as many banks have grown uncomfortable in providing submissions based on expert judgment and may eventually choose to stop submitting altogether.<sup>13</sup> The relatively small number of transactions underpinning LIBOR has been driven by changing market structure, regulatory capital, and liquidity

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<sup>10</sup> As explained in Mortgagee Letter 2021-08, the changes made by the Mortgagee Letter revised the existing HECM regulations pursuant to the authority granted in the Reverse Mortgage Stabilization Act of 2013 (Pub. L. 113–29; Section 255(h)(3) of the National Housing Act (12 U.S.C. 1715z– 20(h)(3))).

<sup>11</sup> The ARRC is a group of private-market participants convened by the Federal Reserve Board and the Federal Reserve Bank of New York to help ensure a successful transition from U.S. dollar (USD) LIBOR to a more robust reference rate, its recommended alternative, the Secured Overnight Financing Rate (SOFR). The ARRC is comprised of a diverse set of private-sector entities that have an important presence in markets affected by USD LIBOR and a wide array of official-sector entities, including banking and financial sector regulators, as ex-officio members. [https:// www.newyorkfed.org/arrc](https://www.newyorkfed.org/arrc).

<sup>12</sup> ARRC Recommendations Regarding More Robust LIBOR Fallback Contract Language for New Closed-End, Residential Adjustable Rate Mortgages, [newyorkfed.org](https://www.newyorkfed.org/medialibrary/Microsites/arrc/files/2019/ARM_Fallback_Language.pdf) (Nov. 15, 2019), [https://www.newyorkfed.org/medialibrary/Microsites/arrc/files/2019/ARM\\_Fallback\\_Language.pdf](https://www.newyorkfed.org/medialibrary/Microsites/arrc/files/2019/ARM_Fallback_Language.pdf).

<sup>13</sup> See Second Report, The Alternative Reference Rates Committee, p.6 (March 2018), <https://www.newyorkfed.org/medialibrary/Microsites/arrc/files/2018/ARRC-Second-report>.

requirements as well as changes in bank risk appetite for short-term funding, thereby creating uncertainty as to the integrity of the index.

In July of 2017, the U.K. Financial Conduct Authority (FCA), the financial regulator of LIBOR, announced that it would no longer persuade or compel contributing banks to submit rates used to calculate LIBOR after December 31, 2021, further heightening the uncertainty of LIBOR.<sup>14</sup> On November 30, 2020, the Federal Reserve Board announced that regulators had proposed clear end dates for the USD LIBOR immediately following the December 31, 2021 publication for the one week and two month USD LIBOR settings, and immediately following the June 30, 2023 publication for other USD LIBOR tenors.<sup>15</sup> On March 5, 2021, the ICE Benchmark Administration Limited (IBA) published the feedback it received to a December, 2020, consultation, and announced it would cease publication of the one month and one year USD LIBOR immediately following the LIBOR publication on June 30, 2023.<sup>16</sup>

With the uncertainty and upcoming phase-out of LIBOR, mortgagees have been working to transition to a new replacement interest rate index for existing ARM contracts. The ARRC, a group of private market participants convened by the Federal Reserve Board and the Federal Reserve Bank of New York to ensure the transition from USD LIBOR to a reliable reference rate, recommended the selection of SOFR for use in new USD contracts.<sup>17</sup> SOFR is published by the Federal Reserve Bank of New York in cooperation with the Office of Financial Research, an independent bureau with the U.S. Department of the Treasury, and “. . . is a broad measure of the cost of borrowing cash overnight collateralized by U.S. Treasury securities in the repurchase

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<sup>14</sup> Andrew Bailey, The Future of LIBOR, Fin. Conduct Authority (July 27, 2017), <https://www.fca.org.uk/news/speeches/the-future-of-libor>.

<sup>15</sup> See Federal Reserve Board Welcomes and Supports Release of Proposal and Supervisory Statements that Would Enable Clear End Date for U.S. Dollar (USD) LIBOR and Would Promote the Safety and Soundness of the Financial System, Board of Governors of the Federal Reserve System (Nov. 30, 2020), <https://www.federalreserve.gov/newsevents/pressreleases/bcreg20201130b.htm>.

<sup>16</sup> ICE LIBOR, Feedback Statement on Consultation on Potential Cessation, ICE Benchmark Admin. (March 5, 2021), [https://www.theice.com/publicdocs/ICE\\_LIBOR\\_feedback\\_statement\\_on\\_consultation\\_on\\_potential\\_cessation.pdf](https://www.theice.com/publicdocs/ICE_LIBOR_feedback_statement_on_consultation_on_potential_cessation.pdf).

<sup>17</sup> About, Alternative Reference Rates Comm., <https://www.newyorkfed.org/arrc/about> (last visited June 10, 2021).

agreement (repo) market.”<sup>18</sup> HUD anticipates that a spread-adjusted SOFR will be published to minimize the impact of the transition on legacy ARMs and other LIBOR-based contracts.

According to the ARRC, “SOFR is suitable to be used across a broad range of financial products, including but not limited to, derivatives (listed, cleared, and bilateral-OTC), and many variable rate cash products that have historically referenced LIBOR.”<sup>19</sup>

As part of the Consolidated Appropriations Act, 2022,<sup>20</sup> Congress passed the Adjustable Interest Rate (LIBOR) Act of 2021 (LIBOR Act)<sup>21</sup> to, in part, create a clear and uniform process, on a nationwide basis, for replacing LIBOR in existing contracts where the terms do not provide for the use of a clearly defined or practicable replacement benchmark rate, without affecting the ability of parties to use any appropriate benchmark rate in a new contract.<sup>22</sup> Generally, for LIBOR-based ARMs without language providing for a specific replacement index, the default replacement index will be a spread-adjusted SOFR as provided for under the LIBOR Act.

The LIBOR Act establishes that this spread-adjusted replacement index will replace LIBOR for existing contracts on the Replacement Date, specified in the LIBOR Act as the first London banking day after June 30, 2023, unless the Federal Reserve Board specifies another date (the “Replacement Date”).<sup>23</sup> The LIBOR Act also established a one-year linear basis to transition the tenor spread adjustment from LIBOR to the SOFR spread-adjusted index.<sup>24</sup> For FHA-insured LIBOR-based ARMs, the LIBOR Act authorizes HUD to approve the spread-adjusted SOFR index, or another benchmark replacement index selected by HUD, as a replacement to LIBOR for existing ARMs starting on the Replacement Date.<sup>25</sup>

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<sup>18</sup> Transition from LIBOR, Alternative Reference Rates Comm., <https://www.newyorkfed.org/arrc/sofr-transition> (last visited June 10, 2021).

<sup>19</sup> Frequently Asked Questions, Alternative Reference Rates Comm (April 21, 2021), <https://www.newyorkfed.org/medialibrary/Microsites/arrc/files/ARRC-faq.pdf>.

<sup>20</sup> Consolidated Appropriations Act, 2022, Pub. L. No. 117-103.

<sup>21</sup> *Id.* at Division U.

<sup>22</sup> *Id.* at Division U, Section 102(b)(1).

<sup>23</sup> *Id.* at Division U, Section 103(6), (17), (19) and Section 104(a)(3)).

<sup>24</sup> *Id.* at Division U, Section 104(e)(2).

<sup>25</sup> *Id.* at Division U, Section 103(10) and Section 104(c).



On October 5, 2021, HUD published an advanced notice of proposed rulemaking (ANPR) to seek input from the public on the transition away from LIBOR.<sup>26</sup> HUD sought comment on how to address a Secretary-approved replacement index for existing loans and provide for a transition date consistent with the cessation of the LIBOR index. HUD also sought comment on replacing the LIBOR index with the SOFR interest rate index, with a compatible spread adjustment to minimize the impact of the replacement index for existing ARMs. The comment period closed on December 6, 2021. HUD received nine comments on the ANPR. Comments were mostly supportive of transitioning away from LIBOR and multiple commenters specifically suggested the use of SOFR as a replacement index. Commenters also provided suggestions on how to smoothly transition off LIBOR. HUD has considered these comments in drafting this proposed rule.

## **II. This proposed rule**

HUD proposes three changes. First, HUD proposes to transition from LIBOR to a spread-adjusted SOFR index for existing forward and HECM ARMs, and to replace LIBOR with SOFR as a Secretary-approved index for new ARMs. Second, HUD proposes to clarify its regulations regarding the Monthly Adjustable Interest Rate HECMs at § 206.21(b)(2). Third, HUD proposes to establish a five percentage point lifetime cap on the adjustment of the HECM monthly ARM interest rate.

### **A. Transition from LIBOR to SOFR §§ 203.49, 206.21.**

This proposed rule addresses both the transition from LIBOR to SOFR for new forward ARM originations and the transition from LIBOR to a spread-adjusted SOFR index for existing forward and HECM ARMs. This proposed rule would also update the HECM ARM regulation

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<sup>26</sup> 86 FR 54876.

consistent with changes already made through Mortgagee Letter 2021-08 regarding new originations.

New originations for forward and HECM ARM. §§ 203.49(b)(1), 206.21(b)(1)(ii)(A).

HUD is proposing to remove LIBOR and approve SOFR as a Secretary-approved interest rate index for FHA-insured ARM. CMT would continue to be a Secretary-approved interest rate, and this rule would provide that both CMT and SOFR may be used for periodic adjustments for newly-originated forward ARM.

As discussed above, HUD, through Mortgagee Letter 2021-08, has already removed LIBOR and approved SOFR as a Secretary-approved interest rate index for HECM ARM closed on or after May 3, 2021. This proposed rule would align forward ARM indices with the change made by Mortgagee Letter 2021-08. HUD is also proposing to update § 206.21(b)(1)(ii)(A) so that HUD's HECM ARM regulations are consistent with the changes made by Mortgagee Letter 2021-08. These changes include establishing zero as the minimum for the index value used to determine the mortgage interest rate for all HECMs to prevent against below-zero interest rates in a negative interest rate environment.

This rule proposes to use the 30-day average SOFR tenor adjusted to a constant maturity of one year. However, HUD anticipates that it may decide to approve additional SOFR tenors besides the 30-day average when additional SOFR tenors are published or more information about existing tenors is made available. Therefore, for both forward and HECM mortgages, HUD is also proposing that HUD may approve alternative SOFR tenors for new originations through notice.

Transition from LIBOR for existing forward and HECM mortgages. §§ 203.49(b)(2), 206.21(b)(1)(ii)(B).

For existing forward and HECM ARM using LIBOR, HUD proposes to require that, on the Replacement Date, ARM currently using LIBOR for their annual or monthly adjustments, as applicable, transition to the spread-adjusted SOFR index as specified in the LIBOR Act. This

spread-adjusted SOFR would be the only Secretary-approved replacement index for transitioning existing forward and HECM LIBOR-based ARMs. HUD also proposes requiring that mortgagees provide notice to the borrower of the replacement in accordance with the terms of the loan documents.

Before the Replacement Date, the loan documents for these mortgages govern the terms of the loan and, as long as the LIBOR index is available, mortgagees may not have flexibility to substitute a new index without a modification of the existing loan documents or executing new loan documents. However, the LIBOR Act specifies that, on the Replacement Date, mortgagees will no longer be required to use LIBOR and must instead use a replacement index.

HUD anticipates that possible fluctuations in the interest rate from the transition to the spread-adjusted SOFR would be tempered by FHA's existing per-adjustment or life of mortgage caps set forth in the mortgage documents or FHA regulations.<sup>27</sup> Additionally, using the tenor spread adjustment as provided for in the LIBOR Act would further help to mitigate impacts due to the transition because this spread adjustment is intended to create as little disruption as possible during the transition. Furthermore, the applicable SOFR tenors will be identified by the Federal Reserve Board prior to the Replacement Date and HUD believes that the spread-adjusted SOFR will provide a comparable interest rate consistent with the rate that would have been generated by the LIBOR index.

HUD also proposes that the Secretary will publish through notice any additional requirements for transition of existing LIBOR-based ARMs to address technical aspects of the transition process, newly published SOFR tenors, and any developments arising from the transition.

## **B. Monthly Adjustable Interest Rate HECMs § 206.21(b)(2)**

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<sup>27</sup> These caps are set forth in Section 251 of the National Housing Act (12 U.S.C. 1715z-16) for insured forward ARMs and Section 255 of the National Housing Act (12 U.S.C. 1715z-20) for annually adjustable HECMs. See also, §§ 203.49(f), § 206.21(b)(1)(iv).

When HUD issued its HECM final rule in January 2017, HUD removed cross references to 24 CFR part 203 and added specific language to discuss the annual adjustments for HECM ARMs, but did not include the same level of specific structure for monthly adjustments.<sup>28</sup> HUD is proposing to restructure § 206.21(b)(2) to clarify the requirements applicable to monthly adjustments to align with those provided for annual adjustments.

### **C. Five Percent Lifetime Cap § 206.21(b)(2)(iii)**

HUD proposes a limit on the adjustment of the HECM ARM monthly interest rate in either direction of no more than five percentage points from the initial contract interest rate. This change would align with similar ARM interest rate caps that are currently used for annual interest rate HECMs and forward ARMs in the mortgage industry. This proposal would reduce risk to the borrower and the Mutual Mortgage Insurance Fund (MMIF) by reducing potential loan balance growth.

### **III. 30-Day Public Comment Period**

In accordance with HUD's regulations on rulemaking at 24 CFR part 10, it is HUD's policy that the public comment period for proposed rules should be 60 days. In the case of this proposed rule, however, HUD has determined there is good cause to reduce the public comment period to 30 days.

HUD's October 5, 2021, ANPR sought 60 days of public comment on alternate indexes and best methods of transitioning off LIBOR. HUD received nine comments in response to HUD's ANPR that were generally supportive of the course of action HUD now proposes in this rule.

After HUD published its ANPR, Congress passed and the President signed into law the LIBOR Act, which provides for a clear and uniform nationwide process for replacing LIBOR in existing contracts. The LIBOR Act answered many of the questions that were uncertain at the time when HUD published its ANPR.

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<sup>28</sup> 82 FR 7094, January 19, 2017.

HUD believes the LIBOR Act, which HUD's proposed rule would implement, creates such an overwhelming industry standard that few if any questions remain regarding how HUD should proceed. HUD also believes that the comments received in response to its ANPR indicate that 30 days is sufficient time for commenters to consider and respond to this proposed rule.

HUD also believes that, with the discontinuation of LIBOR due for June 30, 2023, a 30-day comment period would aid HUD in moving toward a final rule as quickly as possible. Providing more time between the final rule and the discontinuation of LIBOR would ease the transition off LIBOR by ensuring that the regulatory structure and necessary guidance is in place to transition existing forward and HECM ARMs to a spread-adjusted replacement index, and to allow for the origination of new forward ARMs on a replacement index by June 30, 2023.

Given the above justifications, HUD believes that good cause exists to reduce the public comment period to 30 days. All comments received during the 30-day public comment period will be considered in the development of the final rule.

#### **IV. Findings and Certifications**

##### **Regulatory Review—Executive Orders 12866 and 13563**

Under Executive Order 12866 (Regulatory Planning and Review), a determination must be made whether a regulatory action is significant and, therefore, subject to review by the Office of Management and Budget (OMB) in accordance with the requirements of the Order. Executive Order 13563 (Improving Regulations and Regulatory Review) directs executive agencies to analyze regulations that are “outmoded, ineffective, insufficient, or excessively burdensome, and to modify, streamline, expand, or repeal them in accordance with what has been learned. Executive Order 13563 also directs that, where relevant, feasible, and consistent with regulatory objectives, and to the extent permitted by law, agencies are to identify and consider regulatory approaches that reduce burdens and maintain flexibility and freedom of choice for the public.

The current rules providing for the use of LIBOR as an index for interest rate adjustments for ARMs in HUD's forward and reverse mortgage insurance programs are becoming obsolete as

LIBOR is in the process of being phased out. HUD is required by statute to approve by regulation interest rate indices for its forward ARM products. HUD must also amend by regulation its permitted interest rate indices for HECM ARM products and permit lenders to transition from LIBOR to a replacement index for existing HECM ARMs. Therefore, this rule is necessary to prevent HUD's rules on ARMs from becoming obsolete as well as to avoid the risk of financial harm for all ARM lenders and borrowers, and the larger ARM market, and the MMIF.

HUD does not expect the rule to have an economic impact as a result of the transition to the alternative rate. For newly endorsed forward ARMs, SOFR will become an available index in addition to the one-year CMT index. HUD has already removed LIBOR and approved SOFR for new annually adjustable HECM ARM originations. As of the Effective Date or prior to the cessation of LIBOR, existing LIBOR indexed FHA-insured ARMs may transition to a spread-adjusted SOFR to make it a comparable rate for existing LIBOR-based ARMs. Transition to the spread-adjusted SOFR will align FHA-insured ARMs with other LIBOR contracts covered by the LIBOR Act.

For existing mortgages that transition to spread-adjusted SOFR, we do not anticipate a significant economic impact. For all existing FHA-insured ARMs, the per-adjustment and lifetime caps on total adjustments will continue to apply, minimizing the impact to borrowers or mortgagees as a result of the transition to SOFR.

This rule was not subject to OMB review. This rule is not a "significant regulatory action" as defined in Section 3(f) of Executive Order 12866, and is not an economically significant regulatory action.

#### Unfunded Mandates Reform Act

Title II of the Unfunded Mandates Reform Act of 1995 (Pub. L. 104-4; approved March 22, 1995) (UMRA) establishes requirements for federal agencies to assess the effects of their regulatory actions on state, local, and tribal governments, and on the private sector. This

proposed rule would not impose any federal mandates on any state, local, or tribal governments, or on the private sector, within the meaning of the UMRA.

#### Environmental Review

This proposed rule consists of “[s]tatutorily required and/or discretionary establishment and review of interest rates, mortgage limits, building cost limits, prototype costs, fair market rent schedules, HUD-determined prevailing wage rates, income limits and exclusions with regard to eligibility for or calculation of HUD housing assistance or rental assistance, and similar rate and cost determinations and related external administrative or fiscal requirements or procedures which do not constitute a development decision that affects the physical condition of specific project areas or building sites.” Accordingly, under 24 CFR 50.19(c)(6), this proposed rule is categorically excluded from environmental review under the National Environmental Policy Act of 1969 (42 U.S.C. 4321).

#### Regulatory Flexibility Act

The Regulatory Flexibility Act (RFA) (5 U.S.C. 601 et seq.) generally requires an agency to conduct a regulatory flexibility analysis of any rule subject to notice and comment rulemaking requirements, unless the agency certifies that the rule will not have a significant economic impact on a substantial number of small entities. This rule would provide for the removal of LIBOR as an allowable index rate for adjustments for new FHA-insured forward ARMs and establish SOFR as a new index along with the CMT for new forward ARMs, aligning it with the available indices for annually adjustable HECM ARMs. There would be a Secretary-approved spread-adjusted SOFR for existing FHA-insured ARMs transitioning from LIBOR.

The change of this proposed rule requires mortgagees to, where appropriate, utilize a new approved index. Mortgagees are already required to substitute an index under the terms of their existing loan documents when the index used becomes unavailable. Additionally, this proposed rule establishes a new index for origination of new forward ARMs, which mortgagees regularly provide when originating a loan. Therefore, the changes in this proposed rule should not have a

significant economic impact on mortgagees. If there is an economic effect on mortgagees, it would fall equally on all mortgagees who originate or service ARMs. Further, HUD anticipates that allowing an additional index for newly originated ARMs would have a net positive economic impact on borrowers and mortgagees by providing additional market opportunities, decreasing the cost of credit associated with these ARMs.

Therefore, the undersigned certifies that the rule will not have a significant economic impact on a substantial number of small entities. Notwithstanding HUD's determination that this rule will not have a significant effect on a substantial number of small entities, HUD specifically invites comments regarding any less burdensome alternatives to this rule that will meet HUD's objectives as described in the preamble to this rule.

#### Executive Order 13132, Federalism 64 FR 43255; August 10, 1999

Executive Order 13132 (entitled "Federalism") prohibits an agency from publishing any rule that has federalism implications if the rule either: (1) imposes substantial direct compliance costs on State and local governments and is not required by statute, or (2) preempts State law, unless the agency meets the consultation and funding requirements of section 6 of the Executive Order. This proposed rule does not have federalism implications and does not impose substantial direct compliance costs on State and local governments or preempt State law within the meaning of the Executive order.

#### Paperwork Reduction Act

The information collection requirements contained in this proposed rule are currently approved by OMB and have been given OMB Control Number 2502-0322 and OMB Control Number 2502-0524 and 2502-0611. In accordance with the Paperwork Reduction Act, an agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection displays a currently valid OMB control number.

#### **List of Subjects**

#### **24 CFR Part 203**



Hawaiian Natives, Home improvement, Indians—lands, Loans programs—housing and community development, Mortgage insurance, Reporting and recordkeeping requirements, Solar energy.

## **24 CFR Part 206**

Aged, Condominiums, Loan programs—housing and community development, Mortgage insurance, Reporting and recordkeeping requirements.

For the reasons stated in the preamble, HUD proposes to amend 24 CFR parts 203 and 206 as follows:

### **PART 203—SINGLE FAMILY MORTGAGE INSURANCE**

1. The authority citation for part 203 continues to read as follows:

**Authority:** 12 U.S.C. 1707, 1709, 1710, 1715b, 1715z-16, 1715u, and 1715z-21; 15 U.S.C. 1639c; 42 U.S.C. 3535(d).

2. Amend § 203.49 by revising paragraph (b) to read as follows:

#### **§ 203.49 Eligibility of adjustable rate mortgages.**

\* \* \* \* \*

*(b) Interest-rate index. (1) CMT and SOFR Indices.* Changes in the interest rate charged on an adjustable rate mortgage must correspond either to changes in the weekly average yield on U.S. Treasury securities, adjusted to a constant maturity of one year (CMT); to the 30-day average Secured Overnight Financing Rate (SOFR) published by the Federal Reserve Bank of New York (or a successor administrator), adjusted to a constant maturity of one year; or to an alternative SOFR tenor approved by the Secretary. The Secretary may publish approved SOFR tenors as alternatives to the 30-day SOFR tenor through notice.

*(2) Transition for existing mortgages indexed to LIBOR.* Mortgages with an existing adjustable interest rate indexed to the London Interbank Offered Rate (LIBOR) must be transitioned to the spread-adjusted SOFR replacement index approved by the Secretary by the

next interest rate adjustment date for the mortgage on or after the Replacement Date, which means the first London banking day after June 30, 2023, unless the Board of Governors of the Federal Reserve System determines that any LIBOR tenor will cease to be published or cease to be representative on a different date. In such case, Replacement Date means the first business day following the date announced by the Board of Governors of the Federal Reserve System. Notice of the transition to the SOFR replacement index must be sent to the borrower in accordance with the mortgage documents. The Secretary will publish through notice any additional requirements for the transition of existing mortgages.

(3) *Changes in the mortgage interest rate.* Except as otherwise provided in this section, each change in the mortgage interest rate must correspond to the upward and downward change in the index.

\* \* \* \* \*

## **PART 206—HOME EQUITY CONVERSION MORTGAGE INSURANCE**

3. The authority citation for part 206 continues to read as follows:

**Authority:** 12 U.S.C. 1715b, 1715z-20; 42 U.S.C. 3535(d).

### **Subpart A—General**

4. Amend § 206.3 by revising the definition of “Expected average mortgage interest rate” and adding, in alphabetical order, definitions for “Margin”, “Replacement Date”, and “SOFR” to read as follows:

#### **§ 206.3 Definitions.**

\* \* \* \* \*

*Expected average mortgage interest rate* means the interest rate used to calculate the principal limit established at closing.

(1) For fixed interest rate HECMs, the expected average mortgage interest rate is the same as the fixed mortgage (Note) interest rate and is set simultaneously with the fixed interest (Note) rate.

(2) For adjustable interest rate HECMs, the expected average mortgage interest rate is the sum of the mortgagee's margin plus the weekly average yield for U.S. Treasury securities (CMT) adjusted to a constant maturity of 10 years or an additional SOFR index as approved by the Secretary. Commingling the index type used to calculate the expected average mortgage interest rate and the index type used to calculate the adjustable mortgage interest (Note) rate and adjustments is only permissible as provided for by the Secretary.

(3) Mortgagees, with the agreement of the borrower, may simultaneously lock in the expected average mortgage interest rate and the mortgagee's margin prior to the date of mortgage closing or simultaneously establish the expected average mortgage interest rate and the mortgagee's margin on the date of mortgage closing.

\* \* \* \* \*

*Margin* means the amount added to the index value to compute the expected average mortgage interest rate and the initial mortgage interest (Note) rate and periodic adjustments to the mortgage interest (Note) rate.

\* \* \* \* \*

*Replacement Date* means the first London banking day after June 30, 2023, unless the Board of Governors of the Federal Reserve System determines that any LIBOR tenor will cease to be published or cease to be representative on a different date. In such case, Replacement Date means the first business day following the date announced by the Board of Governors of the Federal Reserve System.

*SOFR* means the Secured Overnight Financing Rate published by the Federal Reserve Bank of New York (or a successor administrator).

\* \* \* \* \*

## Subpart B—Eligibility; Endorsement

5. Amend § 206.21 by revising paragraphs (b)(1)(ii) and (b)(2) to read as follows:

### § 206.21 Interest rate.

\* \* \* \* \*

(b) \* \* \*

(1) \* \* \*

(ii) *Interest rate index. (A) CMT and SOFR Indices.* Changes in the mortgage interest rate charged on an adjustable interest rate mortgage must correspond to changes in the weekly average yield on U.S. Treasury securities (CMT) adjusted to a constant maturity of one year; to the 30-day average Secured Overnight Financing Rate (SOFR) adjusted to a constant maturity of one year; or to an alternative SOFR tenor approved by the Secretary. The Secretary may publish approved SOFR tenors as alternatives to the 30-day SOFR tenor through notice. The index type used to calculate the initial mortgage interest rate must be the same index type used to calculate the mortgage interest rate adjustments, except as provided in (B) of this section. Commingling of index types for the mortgage interest rate and adjustments is not otherwise allowed, unless approved by the Secretary. Unless otherwise provided in this section, each change in the mortgage interest rate must correspond to the upward and downward change in the index, except that downward changes in the index will not result in a mortgage interest rate that is less than zero.

(B) *Transition for existing mortgages indexed to LIBOR.* Mortgages with an existing adjustable interest rate indexed to the London Interbank Offered Rate (LIBOR) must be transitioned to the spread-adjusted SOFR replacement index approved by the Secretary by the next interest rate adjustment date for the mortgage on or after the Replacement Date. Notice of the transition to the SOFR replacement index must be sent to the borrower in accordance with the mortgage documents. The Secretary will publish through notice any additional requirements for the transition of existing mortgages.

(2) *Monthly adjustable interest rate HECMs.* If a mortgage meeting the requirements of paragraph (b)(1) of this section is offered, the mortgagee may also offer a mortgage which provides for monthly adjustments to the interest rate subject to the following requirements:

(i) *Interest Rate Index.* Changes in the interest rate charged on an adjustable interest rate mortgage shall correspond to changes in the weekly average yield on U.S. Treasury securities (CMT) adjusted to a constant maturity of one year, to the weekly average yield on CMT adjusted to one-month, or to an alternative SOFR index approved by the Secretary. The index type used to calculate the initial mortgage interest rate must be the same index type used to calculate the mortgage interest rate adjustments, except as provided in (b)(1)(ii)(B) of this section.

Commingling of index types for the mortgage interest rate and adjustments is not otherwise allowed, unless approved by the Secretary. Unless otherwise provided in this section, each change in the Note rate must correspond to the upward and downward change in the index, except that downward changes in the index will not result in a Note rate that is less than zero.

(ii) *Frequency of interest rate changes.*

(A) The interest rate adjustments must occur monthly, calculated from the date of the closing, except that the first adjustment shall be no sooner than 30 days (28 days for February, as applicable) or later than three months from the date of the closing.

(B) To set the new interest rate, the mortgagee will determine the change between the initial (*i.e.*, base) index figure and the current index figure, or will add a specific margin to the current index figure. The initial index figure shall be the most recent figure available before the date of mortgage loan origination. The current index figure shall be the most recent index figure available 30 days (28 days for February, as applicable) before the date of each interest rate adjustment.

(iii) *Magnitude of Changes*. The initial mortgage interest rate shall be agreed upon by the mortgagee and the borrower. Adjustments in the effective rate of interest over the entire term of the mortgage may not result in a change in either direction of more than five percentage points from the initial contract interest rate.

\* \* \* \* \*

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Julia R. Gordon,  
Assistant Secretary for Housing - FHA  
Commissioner.

**Billing code: 4210-67**

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